

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Alliant Energy Corporate Services, Inc.)	
(on behalf of IES Utilities, Inc. and)	
Interstate Power Company),)	
American Transmission Company LLC,)	
Central Illinois Light Company,)	
Cinergy Corp.)	
(on behalf of Cincinnati Gas & Electric Co.,)	Docket No. RT01-96-000
PSI Energy, Inc., and Union Light, Heat & Power),)	
Hoosier Energy Rural Electric Coop., Inc.,)	
Kentucky Utilities Company,)	
Louisville Gas & Electric Company,)	
Northern States Power Company (Minnesota),)	
Northern States Power Company (Wisconsin),)	
Southern Indiana Gas & Electric Company, and)	
Upper Peninsula Power Company)	

**COMMENTS OF THE
ILLINOIS COMMERCE COMMISSION**

I. INTRODUCTION

Pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.211, and the Commission's January 26, 2001 and February 6, 2001, Notices of Filing, the Illinois Commerce Commission ("ICC") hereby submits its Comments in the above captioned proceeding.

II. BACKGROUND

On January 16, 2001, the companies listed above ("Specified Transmission Owners") submitted for filing certain documents intended to satisfy their compliance filing obligations under Order

Nos. 2000 and 2000-A (“Specified Transmission Owners’ Filing”). On January 31, 2001, the Specified Transmission Owners submitted an errata to their January 16, 2001 filing to add the Upper Peninsula Power Company as one of the Specified Transmission Owners participating in that filing.

III. ICC POSITION AND RECOMMENDATION

The Specified Transmission Owners, all of whom are signatories to the Midwest ISO Agreement, state in their filing that the Midwest ISO satisfies the Commission’s Order 2000 RTO characteristics and functions. Specified Transmission Owners’ Filing at 3-4. The ICC, however, disagrees that the filing satisfies the following requirements of Order 2000:

- ?? Order 2000 requires that the RTO have the independent and exclusive right to make Section 205 filings that apply to the rates, terms, and conditions of transmission services over the facilities operated by the RTO. The Midwest ISO Agreement, however, reserves this right to the transmission-owning utilities.
- ?? Order 2000 requires the RTO to be of proper scope and configuration. The Midwest ISO, however, is of insufficient scope and configuration to obtain the Order 2000 standards concerning facilitation of competitive markets and internalization of parallel flows.
- ?? Order 2000 requires the RTO to have "operational control." The Midwest ISO Agreement, however, preserves the rights of transmission-owning utilities to perform the control area operator functions and does nothing to phase out this aspect of utility operational control.
- ?? Order 2000 requires the RTO to provide non-discriminatory service. The Midwest ISO Agreement, however, does not require bundled retail load (without the choice to be unbundled) to be under the Midwest ISO tariff until the end of a six-year transition period. That is discriminatory to Illinois load, all of which will be under the Midwest ISO tariff as of May 1, 2002.

Accordingly, the ICC requests that the Commission modify these provisions of the Midwest ISO Agreement and the Midwest ISO OATT to conform with Order 2000 as described below. Without such modifications, the Midwest ISO cannot be found to be Order 2000-compliant.

In addition, the Specified Transmission Owners describe proposed “innovative” revisions to the Midwest ISO transmission rates and rate methodology. These proposals are not properly before the Commission under Order 2000 and the Specified Transmission Owners have failed to provide proper support for the proposed revisions. Therefore, the Commission should not act on these proposals unless and until they are properly filed.

IV. DISCUSSION

A. The RTO Must Have Independent and Exclusive Authority Over Its Rates, Terms, and Conditions

In Order 2000-A, the Commission stated as follows:

[I]n the ISO type of situation, the RTO [must] have the independent and exclusive right to make Section 205 filings that apply to the rates, terms, and conditions of transmission services over the facilities operated by the RTO, but that transmission owners have the right to make Section 205 filings to determine the appropriate payments for the RTO’s use of their facilities.

III FERC Stats & Regs ¶31,092 at 31,370. However, Article Two, Section 9, Paragraph C7 of the Midwest ISO Agreement states as follows:

The pricing approach set forth in Appendix C to this Agreement for the “Transition Period,” as defined in such Appendix C, shall not be changed except by unanimous approval of the Owners. After the Transition Period, the pricing approach set forth in such Appendix C may be changed by a three-fourths (3/4) affirmative vote of the Owners with each Owner having one vote.

The Midwest ISO Agreement violates the requirement of Order 2000 in several ways.

The referenced “pricing approach” involves rates, terms, and conditions which would be the subject of Section 205 filings. Therefore, during the transition period, the Midwest ISO will not have the “independent and exclusive right to make Section 205 filings that apply to the rates, terms, and conditions of transmission services over the facilities operated by the RTO” as required by Order 2000.

Even after the transition period, the Midwest ISO will not have the “independent and exclusive right to make Section 205 filings that apply to the rates, terms, and conditions of transmission services over the facilities operated by the RTO” as required by Order 2000. The Commission must remove these restrictions on the Midwest ISO. Otherwise, the Midwest ISO cannot be independent of the transmission owners as required by Order 2000. Moreover, even if the Commission were to make some exceptions to its Order 2000 rule requirements in this regard during a transition period, it would be particularly egregious for the Midwest ISO not to have the independent and exclusive right to establish its own rates, terms, and conditions to be put in place at the conclusion of the transition period. Yet that is precisely what the Midwest ISO Agreement provides for in Article Two, Section 9, Paragraph C7 of the Midwest ISO Agreement.

In any event, the six year transition period established in the Midwest ISO Agreement is far too long. In this regard, the transition period proposed by the Alliance companies, which is scheduled to end on December 31, 2004, is much more reasonable. The ICC suggests that, should the Commission permit the Midwest ISO to retain a transition period, that such transition period be no longer than that which the Commission approves for the Alliance RTO.

B. The RTO Must be of Proper Scope and Configuration

Order 2000 requires that an RTO must serve a region of “sufficient scope and configuration to permit the Regional Transmission Organization to maintain reliability, effectively perform its required functions, and support efficient and non-discriminatory power markets.” 18 C.F.R. §35.34(j)(2). The Specified Transmission Owners state in their filing that “[b]ased on its current membership [that is, with ComEd, Illinois Power, and Ameren included], the Midwest ISO would be of sufficient scope and

regional configuration to conform with this requirement when compared to other similar entities.” Specified Transmission Owners’ Filing at 20 (footnote omitted).

The ICC stated in its Midwest ISO Comments submitted March 16, 1998 that “the nine-owner ISO as filed on January 15, 1998, is of sufficient geographic scope to form a viable RTO.” ICC Comments at 3 (underlining added). However, the ICC also stated that such a geographic configuration is “far from ideal for an ISO in the Midwest Region.” Id. The same can be said about the Midwest ISO geographic scope and configuration on which the Specified Transmission Owners are now basing their geographic sufficiency attestation. It is far from ideal.

Furthermore, the ICC does not agree with the Specified Transmission Owners that the Midwest ISO, even with ComEd, Illinois Power, and Ameren in it, satisfies the scope and configuration requirement of Order 2000. In particular, the Midwest ISO scope and configuration fails to internalize loop flow over a large region and does not thwart the exercise of market power or facilitate the broadest possible energy trading area as required by Order 2000. III FERC Stats & Regs ¶31,092 at 31,082.

With respect to loop flow, the Specified Transmission Owners candidly admit that, “The current configuration of the Midwest ISO does not resolve all loop flow or competition issues in the Midwest.” Specified Transmission Owners’ Filing at 20 fn. 28. The Midwest ISO states that its size will permit it to internalize most, but not all, of the “parallel path flows in its scheduling and pricing process within a region.” Midwest ISO Order 2000 Compliance Filing at 59.

With respect to facilitating the “broadest possible energy trading area,” the testimony of Dr. Peter Fox-Penner, who was, at the time (1998), testifying for the Midwest ISO companies, including Ameren, Illinois Power and ComEd, persuasively explained how inadequate scope and configuration in

the RTO can hinder the development of seamless market development. Direct Testimony of Dr. Peter Fox-Penner in Dkts. ER98-1438 and EC98-24 at 28 (Feb. 6, 1998). Mr. Fox-Penner advocated the inclusion of substantially all of the MAIN and ECAR utilities in the same RTO. Id. at 4-5. “Efficient and non-discriminatory power markets” cannot optimally develop given the dis-aggregated and incomplete geographic configuration of the proposed Midwest ISO. An RTO covering substantially all of the geographic area currently separately covered by the Midwest ISO and the Alliance RTO would satisfy Order 2000’s scope and configuration requirements.

Finally, it is irrelevant for the Specified Transmission Owners to base their geographic sufficiency conclusion on a comparison “to other similar entities.” Specified Transmission Owners’ Filing at 20-21. Similarly, it is irrelevant that the Midwest ISO, as currently configured, “would be the largest ISO in the country.” Id. The applicable geographic scope and configuration standard to be applied in this instance is that set forth in Order 2000. On this score, the Midwest ISO does not measure up.

C. Utility Control Over the Control Area Operator Functions Should be Phased Out

The Midwest ISO Agreement permits the transmission-owning utilities to retain traditional control area operator functions. These include “scheduling and economic dispatch,” and “balanc[ing] load and generation in their control areas.” Midwest ISO Order at 40.

Order 2000 states that “we will not at this time require the RTO to operate what traditionally has been thought of as a single control area for its region.” III FERC Stats & Regs ¶31,089 at 31,091. However, Section 35.34(j)(3) of the rule adopted by Order 2000 requires that the RTO “must have operational authority for all transmission facilities under its control” and that if any operational functions are shared with entities other than the RTO, as is the case here where transmission-owning utilities will retain the traditional control area operator functions, the RTO “must ensure that this sharing of

operational authority will not adversely affect reliability or provide any market participant with an unfair competitive advantage.” 18 C.F.R. §35.34(j)(3). Order 2000 also requires that “the RTO must perform the control functions required to satisfy the minimum characteristics and functions in this Final Rule . . . in a non-discriminatory manner for all market participants” and that “[t]he system of operational control chosen must ensure reliable operation of the grid and non-discriminatory access to the grid by all market participants.” III FERC Stats & Regs ¶31,089 at 31,091.

The Midwest ISO Agreement’s sharing of operating functions that permits transmission-owning utilities to retain control of the control area operator functions does not satisfy Order 2000’s requirements for RTO operational authority. In particular, it does not allow the RTO to “ensure reliable operation of the grid and non-discriminatory access to the grid by all market participants.” Dispersed control area operation unnecessarily complicates RTO real-time balancing and congestion management. With respect to congestion management, the Midwest ISO admits there is no empirical data to indicate how locational marginal pricing would work in a decentralized dispatched region. Midwest ISO Order 2000 Compliance Filing at 55. With respect to real-time balancing, the Midwest ISO admits that, because it will not centrally dispatch, “it has been a challenge for the Midwest ISO to develop a mechanism for determining the market clearing price.” *Id.* at 66. Utility retention of control area operator functions hinders the RTO’s operating authority and permits utilities to maintain barriers to non-discriminatory transmission access.

The ICC recognizes that the immediate consolidation and centralization of all control area operator functions in the RTO may have negative cost consequences. Nevertheless, given the benefits to be obtained, it is reasonable for the Midwest ISO to explore alternatives, as suggested in Order 2000, such as a hierarchical control structure where existing control areas are made subject to RTO

direction. III FERC Stats & Regs ¶31,089 at 31,091. Similarly, the Midwest ISO could phase-in the assumption of control area operator functions over time so as to reach an end-state of control area consolidation by a date certain.

Finally, as the ICC originally requested in its March 16, 1998 Comments to FERC in the Midwest ISO dockets, even if the Commission finds that control area operator functions may remain with the transmission-owning utilities, the Commission should make clear that the Midwest ISO has the authority, upon making appropriate regulatory filings, to assume the control area operator functions from the utilities if and when it finds that step necessary to accomplish its responsibilities under Order 2000. See, ICC Midwest ISO Comments at 31.

D. All Load Should be Under the Tariff

In Order 2000, the Commission stated that, “an RTO will not be successful unless all market participants believe that the RTO will operate the grid and provide transmission service to all grid users on a nondiscriminatory basis.” III FERC Stats & Regs ¶31,089 at 31,065 (underlining added). However, the Midwest ISO Agreement preserves discrimination, at least through the transition period, by not putting all load under the Midwest ISO OATT. In particular, Section II.A.2.a of Appendix C of the Midwest ISO Agreement specifically exempts providers of bundled retail load that does not have “the right to choose a different supplier under a state retail access program or legislation” from taking transmission service under the Midwest ISO OATT to supply that bundled load. In fact, Section II.A.2.c of Appendix C of the Midwest ISO Agreement outright prohibits most transmission owners serving bundled retail load without the right to choose from even electing to put that load under the Midwest ISO OATT. These provisions are clearly discriminatory and in violation of Order 2000.

This feature of the Midwest ISO Agreement is of particular concern to Illinois. Under Illinois law, all commercial and industrial load received the right to choose an alternative supplier on or before January 1, 2001. Indeed, all retail load will acquire the right to choose an alternative supplier by May 1, 2002. Therefore, all Illinois retail load will be under the Midwest ISO OATT in less than six months after Midwest ISO start-up. However, bundled retail load in other Midwest ISO states may not receive the right to choose an alternative supplier prior to the end of the six-year Midwest ISO transition period, and so, would continue to face different conditions for another five and one half years as compared with the Illinois retail load which will all be served under the Midwest ISO OATT. Such an outcome is discriminatory, violates Order 2000, and should not be permitted by the Commission.

E. “Innovative” Transmission Rate Proposals

In Order 2000, the Commission held that it would consider RTOs’ innovative pricing proposals on a case-by-case basis. In this case, the Specified Transmission Owners request that the Commission approve several proposals to revise various aspects of the MISO pricing structure. Specifically, the Transmission Owners request that the Commission approve proposals for (1) direct assignment of the costs of network upgrades and a deferral mechanism to recover costs that can not be currently recovered; (2) the use of a fifteen year depreciation life for new transmission facilities; (3) the use of a 15% return on equity for new transmission facilities; and (4) the adoption of a revenues lost addition to the base transmission rates for the transition period if FERC finds such an approach reasonable in the Alliance filing.

The Specified Transmission Owners claim that they have demonstrated that these rate proposals are just and reasonable and will help to carry out the Commission’s policy goals in Order 2000 and 2000-A. Specified Transmission Owners’ Filing at 48. Nonetheless, the Transmission Owners state

that “[a]t this time, [they] are not submitting revisions under section 205 or 206 of the Federal Power Act to implement these changes.” Id. at 48-49. Rather, the Transmission Owners request Commission approval of the proposals at this time and commit to filing specific tariff language to implement the proposals subsequent to the Commission issuing an order that the proposals are acceptable. Id.

The Commission should not consider the Specified Transmission Owners’ requests to approve these innovative pricing proposals at this time. The Commission was clear in Order 2000 that transmission owners must meet all of the requirements to become an RTO before the Commission will accept any innovative pricing proposals. See, 18 C.F.R. §35.34(e)(providing that “[t]he Commission will consider authorizing any innovative transmission rate treatment ... for an *approved* Regional Transmission Organization”). At this time, the Commission has not approved the Midwest ISO pursuant to Order 2000 and, therefore, the Specified Transmission Owners’ request for approval of their various innovative pricing proposals is premature.

In addition, proposals for innovative pricing must be filed pursuant to section 205 of the Federal Power Act, 16 U.S.C. §824(d). The Commission’s rules provide that “[a]n innovative transmission rate treatment or any other rate proposal made for an *approved* Regional Transmission Organization may be requested as part of any filing that is made under paragraph (d) of this section or in any subsequent rate change proposal under section 205 of the Federal Power Act.” 18 C.F.R. §35.34(e)(4)(emphasis added). Paragraph (d) allows entities to make filings to participate in RTOs “pursuant to sections 203, 205 and 206 of the Federal Power Act,” Id. at §35.34(d)(1), (d)(2), or to petition for a declaratory order that a “proposed transmission entity would qualify as a Regional Transmission Organization.” Id. at §35.34(d)(3). Although in the latter scenario, the petitioners are allowed to make commitments to make filings pursuant to section 203, 205 and 206 of the Federal

Power Act promptly after the Commission issues an order in response to the petition, in this case the latter method for filing an innovating pricing proposal is not applicable because the current filing is not a petition for a declaratory order that the Midwest ISO qualifies as an RTO. As all other methods for making an innovative pricing proposal mandate the filing of the proposals pursuant to section 205 of the Federal Power Act, the Transmission Owners are required to seek review of their proposals pursuant to section 205 in the first instance.

The rationale that underlies the necessity for entities to file innovative pricing proposals pursuant to section 205 of the FPA is quite simple: to ascertain that the applicable statutory standards are satisfied and that parties' due process rights are protected. In particular, the Commission is required to enforce the provisions of its enabling statute, of which section 205 of the FPA is a part, and the parties are entitled to notice of the exact nature and specifics of proposals made pursuant to the statute as well as an opportunity to comment thereon. In this case, however, the Specified Transmission Owners' request would bypass each of these mandates because the Specified Transmission Owners are seeking a Commission order approving their proposals prior to making a filing pursuant to section 205 without providing the specific details of their proposals.

Specifically, while the Specified Transmission Owners set out some over-arching principles for their proposals, the Specified Transmission Owners qualify most statements that could constitute commitments to the details for their proposals that will be filed pursuant to section 205 post-Commission approval. For example, the Specified Transmission Owners consistently utilize terms, such as "contemplate," "anticipate" and "expect," when describing their post-Commission approval section 205 filing that evidence their proposals are far from definite. See e.g., Specified Transmission Owners' Filing at 41 (stating that the Specified Transmission Owners "contemplate that the schedule will not

require the direct assignment of network upgrades in all circumstances”). In addition, the Specified Transmission Owners request approval of their proposals prior to submitting much of the information the Commission stated it would require for a complete review in Order 2000, such as a cost-benefit analysis. While the Specified Transmission Owners state that they will provide cost-benefit data to support a Section 205 filing at a later date, the omission of the date in this filing violates the Commission’s requirement that all innovative pricing proposals filed by RTOs are to be fully and adequately supported in accordance with Order 2000 and the regulatory text. III FERC Stats & Regs ¶31,089 at 31,191.

Accordingly, while the ICC supports the objective that the Specified Transmission Owners claim that the rate proposals are designed to promote - the mitigation of disincentives associated with the planning and construction of necessary transmission upgrades, the ICC requests that the Commission decline to review the Specified Transmission Owners proposals within the context of this compliance filing. Order 2000 states that if industry participants need further guidance from the Commission regarding innovative rate structures, they are to make such requests through declaratory orders or further rulemakings. III FERC Stats & Regs ¶31,089 at 31,191. The ICC requests that the Commission direct the Specified Transmission Owners to make such filings if the Specified Transmission Owners are seeking further Commission guidance prior to making their proposals within the context of the appropriate section 205 filings.

Nonetheless, if the Commission decides to evaluate the Specified Transmission Owners’ proposals within the context of this compliance filing, the ICC still recommends that the Commission decline to adopt the proposals. Section 35.34(e)(1)(iii) of the Commission’s regulations places the burden of proving that any innovative rate proposal is not unduly discriminatory or preferential on the

applicant. This filing has failed to meet this standard and, on its face, appears to be potentially discriminatory. For example, the proposed Attachment N would assign the costs of new network facilities directly to the customer that caused the construction of the facilities. While the Specified Transmission Owners state that all customers will be treated comparably, they also include a provision giving the transmission provider the option of choosing direct assignment or the rolling-in of facilities. Specified Transmission Owners' Filing at 41. Such a provision would allow similar customers to be treated differently subject to the desire of a specific transmission owner. The Commission should reject this provision.

In Order 2000, the Commission made it clear that transmission pricing must still reflect the cost of providing transmission service. III FERC Stats & Regs ¶31,089 at 31,173. The Commission reaffirmed this principle in Order 2000-A. III FERC Stats & Regs ¶31,092 at 31,389. The Specified Transmission Owners' request to include as part of their base rates, a "Lost Revenue" charge to recover revenues that are lost when they transfer operational control to the Midwest ISO violates this principle. Specified Transmission Owners' Filing at 47. Such a provision is not based on cost of service. Instead it is a charge based on revenues in an arbitrarily selected test year. Furthermore, the Specified Transmission Owners had the opportunity to raise their concerns about the loss of these revenues prior to the signing of the Midwest ISO Agreement, yet they raised them only after a mechanism for recovery of such lost revenues was proposed in the Alliance Companies' filing. The Specified Transmission Owners have not demonstrated that inclusion in transmission rates of a lost revenue recovery mechanism is necessary to obtain RTO formation, nor have they adequately supported their specific rate request.

Similarly, the Specified Transmission Owners have not adequately supported their request for a 15% return on equity or to shorten the depreciation period for facilities to 15 years. The ICC is concerned that the inclusion of such features in transmission rates will increase rates without delivering any real benefits to consumers. In addition, the inclusion of such features may discourage the development of a competitive retail and wholesale electric market in the Midwest.

The Specified Transmission Owners request that the Commission accept their proposal to file a mechanism for deferral of the costs of new transmission facilities. This request is based primarily on the existence of retail rate freezes that prevent retail rates from being adjusted to reflect the utilities' incurrance of new costs during the period of the freeze. The Commission should not accept such a proposal. Retail rate freezes were generally adopted by state officials and utilities as part of a package constituting multiple trade-offs. Utilities should not now be permitted by the Commission to escape the bargain that they struck with state officials.

The Commission's regulations expressly limit the consideration of innovative rate proposals to approved RTOs. III FERC Stats & Regs ¶31,089 at 31,191. Furthermore, the ICC concurs with Commissioner Massey's dissent in the International Transmission Company Order where he stated "[t]he straightforward theory of our RTO rule is that the social benefits that flow from RTOs may justify higher rates ... [t]hus innovative rate treatments should be put in effect only when society realizes the benefits of a particular RTO." International Transmission Company, 92 FERC ¶61,276 at 61,918 (2000). To date the consumers of the Midwest have not realized any benefits from the Midwest ISO. In addition, the Commission has yet to find that the Midwest ISO has satisfied the minimum characteristics and functions of Order 2000. As a result, the ICC urges the Commission not to grant the rate requests sought by the Specified Transmission Owners in Section IV of their filing (pages 37-

48) without prejudice to it being refiled when the Specified Transmission Owners are members of an approved operational RTO.

V. CONCLUSION

WHEREFORE, for each and all of the foregoing reasons, the Illinois Commerce Commission respectfully requests that the Commission modify the provisions of the Midwest ISO Agreement and the Midwest ISO OATT as described above; not accept the Specified Transmission Owners' requests concerning innovative rates in Section IV of their filing; and for any and all other appropriate relief.

March 8, 2001

Respectfully submitted,

ILLINOIS COMMERCE COMMISSION

Myra Karegianes
General Counsel and
Special Assistant Attorney General

Sarah A. Naumer
Thomas Aridas
Special Assistant Attorney Generals
Illinois Commerce Commission
160 N. LaSalle, Suite C-800
Chicago, Illinois 60601
(312) 793-2877